The new EC Block Exemption on Technology Transfer Agreements

A new safe harbour from art. 81 (1) EC: The background, market share caps and banned hardcore restraints

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Table of contents

1 INTRODUCTION: WHY LICENSING AGREEMENTS ENCOURAGE COMPETITION 1

2 MODUS OPERANDI 2

2.1 THE AIM OF THIS PAPER 2
2.2 METHOD USED AND SOURCES OF LAW 3

3 ART. 81 AND MODERNISATION: THE NEW REGIME IN EC COMPETITION POLICY 4

3.1 BACKGROUND 4
3.2 ART. 81 (1) EC 6
3.3 SELF-ASSESSMENT: THE NEW APPLICATION OF ART. 81 9

4 REGULATION 772/2004 ON TECHNOLOGY TRANSFER AGREEMENTS 11

4.1 THE HISTORY OF ART. 81(1) AND PATENT LICENSING 11
4.2 THE CONCEPT OF A BLOCK EXEMPTION REGULATION 13
4.2.1 THE MAIN FEATURES AND PURPOSES OF THE TTBE 13
4.3 THE SCOPE OF THE REGULATION 15
4.3.1 PATENTS, KNOW-HOW AND MIXED AGREEMENTS 15
4.3.2 COMPUTER SOFTWARE 16
4.3.3 THE TYPICAL LICENSING AGREEMENT - A SHORT OVERVIEW 17

5 MARKET SHARES AND DEFINITIONS OF THE RELEVANT MARKET 19

5.1 INTRODUCTION: THE *DE MINIMIS* AGREEMENTS 19
5.2 MARKET SHARE CAPS IN THE TTBE, ARTICLE 3 21
5.3 HOW TO DEFINE THE RELEVANT MARKET: MAIN RULE AND THE TTBE-SPECIFIC PROVISIONS 23
5.3.1 MARKET POWER 24
5.3.2 BARRIERS TO ENTRY AND EXIT 25

5.3.3 THE RELEVANT PRODUCT MARKET 26
5.3.3.1 Demand-side substitutability 27
5.3.3.2 Supply-side substitutability 28
5.3.4 THE RELEVANT GEOGRAPHICAL MARKET 29
5.3.5 TTBE: THE RELEVANT PRODUCT *AND* TECHNOLOGY MARKET 30

6 HARDCORE RESTRAINTS 33

6.1 INTRODUCTION 33
6.2 AGREEMENTS BETWEEN COMPETITORS 34
6.2.1 PRICE FIXING 35
6.2.2 LIMITATION OF OUTPUT 37
6.2.3 ALLOCATION OF MARKETS OR CONSUMERS 39
6.2.3.1 Exceptions from the hardcore list in cases similar to market sharing in non-reciprocal agreements 40
6.2.3.2 Field of use and captive use restrictions 41
6.2.3.3 Sole licenses 42
6.2.4 RESTRICTION OF THE USE OF A PARTY'S OWN COMPETING TECHNOLOGY 42
6.2.5 R&D-RESTRICTIONS 43
6.3 AGREEMENTS BETWEEN NON-COMPETITORS 43
6.3.1 PRICE FIXING 44
6.3.2 RESTRICTIONS OF THE LICENSEE'S ACTIVE AND PASSIVE SALES 44
6.3.3 EXCEPTIONS FOR SELECTIVE DISTRIBUTION SYSTEMS 46

7 CONCLUSION 46

8 SOURCES 48

1 Introduction: Why licensing agreements encourage competition

At first glance, the relationship between intellectual property rights (IPR) and competition may seem like a particularly uneasy one. After all, anyone can start selling lemonade, but a certain widget[1] that is patented by a company will confer a de facto, completely legal exclusive monopoly for 20 years to come. Still, economists and competition authorities claim that patents encourage innovation and competition, and bring benefits and lower prices to the consumers. How can this be true?

Firstly, the mere existence of a legal method to protect inventions from illegal copying is believed to be an incentive to spend time and money on research and development. A new drug, for instance, may cost millions of euros and years of research may be spent before it is even introduced on the market. Then it is only fair that the company who made it can exploit it for some years, and if their competitors would like a share of the pie, they would have to make a better drug themselves. This way, companies in the same product market must constantly compete fiercely to be able to hold the rights to the state-of-the-art-product, which will give the consumers the most novel products at the best price. For instance, the patent of a certain way of cleaning music cassettes may still be valid, but not worth a eurocent anymore, since new technology has taken over the product market. Had there not been a legal certainty in patens, companies would probably never have taken on the expensive task of inventing the CD.

Secondly, there have been allegations that patents create lazy monopolists who simply lean back and enjoy the turnaround. This was the topic of an article in *The Economist* recently[2], where is was pointed out that many of the most innovative companies of today have market shares that constitutes a monopoly, which can be seen as a paradox. Some economists claim that wealth in itself, and not necessarily a monopolist position, gives an opportunity and muscles to innovate, constantly keeping competitors at arm's length. At the same time, big companies have "the blessing of

[1] An common term describing an imaginary product. Often used when explaining economic theories.

[2] The Economist Online, published 22 May 2004. www.economist.com

scale" and often better market knowledge, with the ability to read the market in a better way than the smaller, less fortunate widget-producers. This way, they can conduct expensive market surveys, and get to know what the consumers ask for.

In the end, the task for competition authorities will be to balance competition and patents in a way that ensures the legal certainty of a time-limited monopoly in producing the product, at the same time as they will have to intervene if the product is being sold at unreasonable prices. As Mario Monti, the Commissioner for Competition Policy, pointed out in a speech on the new block exemption for technology transfer agreements recently: The task will be to "marry the innovation bride and the competition groom"[3]. Whether or not this task has been fulfilled successfully by the Commission, and especially how the rules are constructed in the new block exemption on technology transfer agreements, will be among the core topics of this paper.

2 Modus operandi

2.1 The aim of this paper

In this paper, I will seek to explain the most important rules that emerged with the brand new Regulation No 772/2004; the new block exemption for technology transfer agreements (from now on dubbed TTBE). Doing so, it will be important to bear in mind the new set of rules in Regulation No 1/2003, the so-called modernisation regulation, that also was brought into force throughout the Community from May 1st. 2004. The latter regulation changes the enforcement of art. 81 and 82 EC[4], and influences the way EC competition policy is to be treated by the companies themselves, especially in terms of exemptions and art. 81(3). At the same time, I will grant some limited space to explain the nature of a EU-regulation and a block exemption in general.

In discussing the new TTBE, focus will be on the shift from the black-, white-, and grey-lists to the new regime implementing market share caps and banned hardcore

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[3] Speech/04/19, Mario Monti, speech at Ecole des Mines, Paris, 16th. January 2004.

[4] All references to the EC Treaty in this paper have numbering introduced by the amended Treaty of Amsterdam.

restraints. I will also focus on the methods used to define the relevant market for the purpose of technology transfer agreements, where both the geographic market, the product market and the technology market need to be defined. Further, the difference between licensing agreements between competitors and non-competitors will be illustrated.

Certain bordering areas of technology transfer agreements will not be debated in this paper: Whether an agreements between an EU-based company and a firm from outside the Union can be subject to EC competition law will not be brought up, nor will detailed IPR-law in general, the drafting of the new European patent directive or certain EEA-spesific questions. Finally, the excluded restrictions in art. 5 of the TTBE will not be dealt with in detail.

2.2 Method used and sources of law

The most important source of law in EC legislation is the Treaty itself. In terms of competition law, art. 81 and 82 are the standout provisions which both deal solely with competition matters. But there are several other articles that can apply in different circumstances, for instance the rules of the four freedoms.

The second most important set of rules are Regulations. According to art. 249 EC, these have been given general application, and will thus be "binding in its entirety and directly applicable in all Member States"[5]. This is in contrast to directives, which as a general rule[6] must be incorporated into national legislation before they can be applied directly and granted direct effect.[7]

In addition, EU-law recognises in art. 249 EC decisions as binding to whom they are addressed, while recommendations and opinions are sources of law that have no binding force. In addition, both the ECJ and the CFI[8] do in fact in a number of cases get inspiration from the case-law of the European Court of Human Rights (ECHR) in Strasbourg, even though this rarely happens on the field of competition. The community

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[5] Art. 249 EC para 2.

[6] As stated in *Dori* (Case C-91/92). See in contrast *CIA* (Case No 194/94).

[7] According to art. 249 EC para 3, directives "shall leave to the national authorities the choice of form and methods".

[8] European Court of Justice and Court of First Instance.

courts also have the final word in disputes concerning the interpretation of EU-legislation.

Apart from the TTBE itself, the Guidelines to the TTBE were published by the Commission parallel with the Regulation. Surely, the Guidelines are of high relevance, as they explain not only the background and the need for a new legal approach, but also set out examples and show how the legality of agreements which no not fall in under the new Regulation are to be examined. However, being a Commission Notice, the Guidelines are not legally binding. This is also true for other Commission Notices used in this paper.

The body of case-law used in this paper is mainly from the Community courts, although other cases may be used to illustrate examples. Because of the need of uniform interpretation, national court decisions will seldom be of a high relevance in EC law.

Writings, books and commentaries from judicial experts will be used in this paper, although these have not been given any formal weight in the treaty. Since TTBE was neither finished nor in force before the end of April and May 1st. 2004[9], literature on this field is rather fragmentary. Therefore, where documents published on-line are used as references, I will use the internet address (URL) in the reference field, and state the date the document was found.

3 Art. 81 and modernisation: The new regime in EC competition policy

3.1 Background

Throughout the decades of enforcement of EC competition rules, the Commission adopted a specific way of granting exceptions from the prohibition rules in the competition provisions. Judging from art. 81(1), a vast majority of cooperation agreements made both between competitors and non-competitors would be deemed illegal, and thus also void after art. 81(2). And although the Commission and the ECJ indeed developed a rather strict interpretation of the prohibition, the reality was

[9] The final Regulation is marked "done at Brussels, 27 April 2004", only few days before it was due to be in force.

somewhat different; many agreements were not harmful to competition, either because these were made between companies with a minimal market share, or the agreements simply did not have the effect of distorting competition.

The Commission have for many years had the possibility of giving so-called individual exemptions after art. 81(3), based on the general legal idea that a general rule cannot be applied when the considerations behind that very same rule does not materialise themselves in a particular case. The main problem with exemptions to the EC competition rules, however, was the fact that the Commission was given a monopoly of grating the exemptions after Regulation 17/62. The idea was that companies who believed they where about to enter an agreement possibly infringing art. 81(1), could apply for an exemption, and then get one within a reasonable time-frame, if the Commission found no hardcore restrictions or other real threats to competition inherent in the agreement.

This approach of gathering of all powers in the hands of the Commission proved to be somewhat of a failure. An insecure competition environment emerged, where companies in the then 15 member states received a so-called "letter of comfort" from the Commission upon applying for an exemption after art. 81(3). This document was barely a *presumption* that the agreement in question probably was not contrary to art. 81(1) (thus satisfying the criteria in art. 81(3)), and had no legal value in itself. In theory, a company could receive a letter of comfort, only to receive a lawsuit lodged before the ECJ by the very same Commission a couple of years later. At the same time, the Commission's workload was enormous, and the applications for exemptions piled up in Brussels.

Come the 1990s, when debate arose on these matters. In 1999, the Commission published a White Paper on Modernisation[10], where it provides a rather simple solution to the pile-up problem; an end to the Commission's exclusive right of granting exemptions to art. 81(1), and an abolition of the whole notification procedure. From now on, the question of determining whether the agreement was anti-competitive or not, shifted to the companies themselves. These are the basics of Regulation 1/2003, which will be discussed later in this chapter.

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[10] OJ [1999] C 132/1.

3.2 Art. 81 (1) EC

Being the most important provision in the field of competition for companies not having a dominant position in the market, art. 81 has a fairly extensive text, filled with terms that must be interpreted. The structure of the article is simple; the prohibition itself is placed in the first paragraph, the somewhat misplaced statement of voidness in paragraph two, and finally the exemptions in paragraph three.

Over the following pages, I will as briefly as possible elaborate the prohibition in art. 81(1). Due to the limited space available in this paper, this is not intended to be a thorough analysis of the enormous body of case-law on this field and different types of agreements caught, though it will have to be mentioned as a background for understanding the exemptions later. The focal point; the block exemption for technology transfer agreements, will be elaborated in detail from chapter 4, together with questions concerning market definitions and the different forms of so-called hardcore restrictions mentioned in art. 8 (1)(a)-(e) which are relevant on the field of technology transfer agreements.

> Art. 81(1) EC reads:
> "1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which:
>
> (a) directly or indirectly fix purchase or selling prices or any other trading conditions;
>
> (b) limit or control production, markets, technical development, or investment;
>
> (c) share markets or sources of supply;
>
> (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

Judging from the wording of art. 81(1) first paragraph, three different forms of cooperation are caught; standard *agreements between undertakings*, *decisions* of an association of undertakings and *concerted practices*.

First of all, the term "undertaking" must be interpreted, as it is not defined in the Treaty itself. According to the jurisprudence of the ECJ, the mere legal status of an undertaking is not important; it is whether or not the entity is engaged in economic activities that is material. In *Höfner*, this is expressed by the Court as "the concept of an undertaking encompasses every entity engaged in an economic activity regardless of the legal status of the entity and the way in which it is financed"[11]. This includes many bodies partly or wholly owned, funded or financed by public authorities, different "clubs" and even FIFA[12].

In addition, art. 81 does not apply to undertakings which are part of the same economic entity, for instance when agreements are made between the parent company and a subsidiary. A so-called "test of control" has been developed in the jurisprudence of the ECJ[13], where different factors such as control over the board of directors in the subsidiary, the flow of profits to the parent company and to what extent the subsidiary follows directions are material. The relationship between a principal and an agent is also normally defined as a single economic entity.

Art. 81(1) apply to both horizontal and vertical agreements, contrary to the popular opinion in the early years of the EC[14]. This means that anti-competitive agreements made between businesses both at the same and different levels of the chain of supply are caught by the provision. However, the market share cap set up in the block

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[11] Case C-41/90 [1991], para 21. Höfner was a case concerning dominance and art. 82, however. See also *Whish* 5th ed., p 81.

[12] OJ [1992] L 326/31 [1994], paras 43-57.

[13] See further Case C73/95P Viho and *Jones and Sufrin* p 103-107.

[14] See in particular Consten and Grundig, Cases 56/84 and 58/64 [1966], as a paramount judgement where vertical agreements were believed to have the ability of infringing art. 81 as well as horizontal agreements.

exemption for vertical agreements (30% of the market share if no hardcore restrictions are found in the agreement), is higher than for horizontal agreements, since the latter types of agreements are generally seen as more destructive.

Furthermore, the borderline between an "agreement" and "concerted practices" is rather vague. If there exists a written agreement between the parties, for instance, the relationship is without question an agreement. But even "understandings" and "Gentleman's agreements" have been defined as agreements for the purpose of art. 81(1). However, the difficulties lay not in determining whether something is an agreement or a concerted practice, since both are included in the prohibition, but rather if it can be labelled collusive or non-collusive behaviour, where the evidence of an agreement lack[15]. An example of the latter can be where the price of products from competitors in the same market area fluctuates more or less coincidentally in the same pattern, which can be a result of price fluctuations on raw materials, or even a simple question of demand. Competing on price is certainly not prohibited. On the other hand, fixing the price is a serious, hardcore restriction, as seen in art. 81(1)(a).

Briefly, when it comes to decisions by associations of undertakings, this part of the prohibition is designed to catch certain collusive activities concluded in different trade associations, co-operatives or other bodies, that are harmful to competition, and yet fall outside the terms of agreement or concerted practices. In general, this part of the prohibition targets the establishment of hidden cartels applying hardcore restrictions as for instance market sharing or price fixing.[16]

Although art. 81(1)(a)-(e) set up a list of anti-competitive behaviour, this is not meant to be exhaustive, as we can read by the very wording "in particular". However, these are viewed as being types of agreements that seriously damages competition. The easiest way of distinguishing hardcore agreements from the rest, is by using the "object/effect"-test. If the agreement has as its very object to prevent, restrict or distort competition, it will often be a hardcore restriction.

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[15] See *Whish* 5th ed. p 94.

[16] Further on the topic, Jones and Sufrin p 118-119 and chapter 11, Whish p 97-99.

3.3 Self-assessment: The new application of art. 81

Regulation 1/2003 art. 1 paragraph 1 and 2 reads:

> 1. Agreements, decisions and concerted practices caught by Article 81(1) of the Treaty which do not satisfy the conditions of Article 81(3) of the Treaty shall be prohibited, no prior decision to that effect being required.
>
> 2. Agreements, decisions and concerted practices caught by Article 81(1) of the Treaty which satisfy the conditions of Article 81(3) of the Treaty shall not be prohibited, no prior decision to that effect being required.

In fairly simple language, the words "no prior decision" change the application of art. 81 for European firms. Earlier, as mentioned, they would have to apply for either a "letter of comfort" or an individual exemption from the Commission. Starting from May 1st. 2004, it is all up to themselves to assess the legality of their agreements. This new regime has caused some anxiety in European firms; many claim that the new rules will introduce more uncertainty. However, the huge delays and "letters of comfort" under the old regime were said to cause uncertainty, frustration and confusion as well. Now, an agreement is either prohibited or legal, as there is no such thing as an individual exemption anymore.

It is crucial to underline that not only the companies themselves, but also national courts and competition authorities now have to power to directly apply the exemptions in art. 81(3), cf. Reg. 1/2003 art. 5 and 6. National competition authorities may also end infringements, order interim measures, accept commitments and impose fines.

When it comes to the self-assessment process, it can be viewed as a four-step procedure. First of all, the company must determine whether the agreement is subject to art. 81(1) in the first place, for instance in cases where an agreement is made between a parent company and a subsidiary, it will not be between undertakings and thus not prohibited by art. 81(1)[17]. The next step will be to search the agreement for possible hardcore restrictions of competition, as these are highly unlikely to be allowed in a non-infringing agreement. Thirdly, block exemptions on the area must be examined, as these

[17] Though it can be an art. 82-infringement, if the company's market share is high.

can serve as a short-cut around a more extensive art. 81(3)-study. For vertical agreements, there is a general block exemption. For more specific agreements, both R&D-agreements, specialisation agreements and technology transfer agreements, to name a few, have their own EC block exemptions. Finally, if legal certainty still has not been achieved, the company must undergo a thorough study of the art. 81(3)-exemption.

Art. 81(3) EC reads:

> The provisions of paragraph 1 may, however, be declared inapplicable in the case of:
>
> - any agreement or category of agreements between undertakings;
>
> - any decision or category of decisions by associations of undertakings;
>
> - any concerted practice or category of concerted practices,
>
> which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:
>
> (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;
>
> (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

The wording "any" [agreement, decision and concerted practice] clearly states that in theory, even hardcore restraints and severely anti-competitive behaviour can satisfy the conditions for exemptions. However, these categories of agreements are usually highly unlikely to do so.[18]

There are four different conditions for an exemption after art. 81(3). Firstly, the agreement must contribute to improving production or distribution of goods or promote a technical or economic process. Secondly, it must let the consumers benefit from these benefits or improvements. Thirdly and fourthly, as seen in art. 81(3)(a) and (b), any restrictions imposed on the party to the agreement must be indispensable, and it must not enable the parties to the agreement to obtain a per se monopoly. These conditions are as mentioned cumulative; they will all need to be fulfilled. For instance, if

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[18] One much used exception is cartel-like cooperation in the form of liner conferences in the Mediterranean Sea, where hardcore market sharing has been allowed by the Commission.

consumers do not benefit from certain improvements, no matter how much the companies save from making the agreements, it will not fulfil the criteria for exemption.

A more extensive analysis on the criteria of exemption after art. 81 (3) will be carried out together with the TTBE-discussion when appropriate over the next chapters.

4 Regulation 772/2004 on Technology Transfer Agreements

4.1 The history of art. 81(1) and patent licensing

The Commission has over the last decades changed its views on the severity of patent licensing clauses and possible infringements of art. 81(1), which is now reflected in the Commission's different block exemptions. This is a short summary.

In the early years of the Community, the Commission's general view was that patent licenses very rarely, if at all, could pose any threats to inter-state competition. This view was mainly based on the thought that, firstly, intra-brand competition was not the primary target in a time where many member states still applied ridiculously protective provisions to hinder the free movement of goods and services, and secondly, because it believed that a high degree of exclusivity on the hands of the both the licensor and the licensee was a necessity in order to even have licensing working as intended. This view changed somewhat after the ECJ-ruling in *Consten and Grundig v Commission*[19], where the Court not only stated that vertical agreements can be caught by art. 81(1), but more importantly in this context, that absolute territorial protection by using IPR-rights, when hindering parallel imports and thus intra-brand competition, could as well have the ability to infringe. The *Consten and Grundig*-case, where Consten as a trade mark licensee had acquired an exclusive right to use the trade mark GINT in France, also established the division between the existence of an IPR-right and the exercise of such a right. This would later pave the way for the famous exhaustion of rights-doctrine by the ECJ, which in short means that once a product is placed on the market by a company which have a legitimate right to do so, the product could as a general rule be sold anywhere in the Community.

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[19] Cases 56/84 and 58/84 [1966] ECR 299, (1966) CMLR 418.

As for territorial protection, the Court hereafter established in a vast number of cases[20] that both non-competition clauses and resale price maintenance, which is the vertical agreements' equivalent to price fixing, were caught by art. 81(1). After a while, a pattern emerged, and the Commission drafted the first block exemption for patent licenses in 1984[21], where the most harmful agreement clauses were blacklisted. This Regulation was later replaced with Regulation 240/96, which also included a 'white list', based on contractual clauses that the Court either did not find infringing, and included licensing of know-how and mixed licenses.

The *Nungesser v Commission*[22]-case, often referred to as 'the Maize Seeds case', further broadened the scope. Here, the question before the Court was whether an exclusive licence of plant breeders' rights had as its object to restrict competition, as referred to in art. 81(1). If this was the case, exclusive licenses would by their very nature infringe art. 81(1), and highly unlikely benefit from the exemption in art. 81(3). The Court distinguished between a sole licence and an exclusive licence, where a sole licence (often referred to as an 'open exclusive licence') merely gives the licensee a guarantee that no licence will be given to a competitor in the same area, whereas an exclusive licence gives absolute territorial protection. The Court decided that a sole licence sometimes was necessary in order to help new companies establish themselves in a new, risky and often young market, at the same time as it did not hinder parallel imports. Therefore, this type of licences was not viewed as having as an object the restriction of competition, thus not being an infringement of art. 81(1). However, the Court did in later cases restrict its own doctrine, as well as the Commission was reluctant to apply the doctrine. *Whish* believes that the Commission would rather like to exempt territorial exclusivity agreements from art. 81(1) using art. 81(3), than "to grant negative clearance under Article 81(1)".[23]

In the last two decades, both the Commission and the Community Courts have focused on the division between agreements having as its object the restriction of competition, and those which can restrict the competition by effect, where the latter often can be exempted under art. 81(3). The introduction of black lists and earlier white

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[20] See Whish p 739, where at least 11 cases are referred to.

[21] Regulation 2349/84

[22] Case 258/78 [1982] ECR 2015, [1983] 1 CMLR 278.

[23] See Whish p 741.

lists in the Commission's different block exemptions can prove this; where severely anti-competitive clauses as for instance price fixing or market sharing are put on the black lists, milder forms of territorial exclusivity are often open for exemption.

4.2 The concept of a block exemption Regulation

A block exemption Regulation is a invention in EC law, where the main purpose is to construct a framework for private companies, enabling them to apply competition rules on a self-regulatory basis. A block exemption is usually aimed at a specific group of agreements which typically can be restrictive of competition, but where the negative sides are outweighed by positive sides and the agreement as a whole will improve economic efficiency and should therefore be exempted, as long as severely anti-competitive restrictions are not included and the market share is under a certain threshold. If the agreement is in line with the block exemption, the parties to the agreement in question will obtain a "safe harbour", and will not be accused of infringing the competition rules. After Reg. 1/2003, when self-assessment as discussed in last chapter became the only solution to get exceptions from art. 81 and 82, block exemptions have become of higher importance than ever before.

In addition, block exemptions are Regulations, which rank them high in the hierarchy of EC provisions, making them directly applicable in the courts of the member states, thus making the enforceability a lot smoother.

4.2.1 The main features and purposes of the TTBE

The TTBE is in many ways a typical EC block exemption. The Regulation itself is fairly short with only 20 recitals and 11 articles, while the Guidelines to the block exemption[24] show the complexity of the field, also granting much space to discuss the interpretation of art. 81(3) on the field of technology transfer agreements in cases where an agreement falls outside the safe harbour of TTBE.

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[24] Guidelines on the application of Article 81 of the EC Treaty to technology transfer agreements, 2004/C 101/02.

The subject matter this block exemption regulates are licensing agreements of certain technology-related IPRs for the purpose of production, and the legality of these in the light of art. 81(1) EC. This block exemption generally works as a safe harbour under art. 81(3) EC, thus enabling the parties to a technology transfer agreement to assess the legality of said agreement without having to launch a deep analysis of art. 81(3). As stated in recital 4 to the TTBE, the overall aim of even constructing a block exemption on this field, is partly to "ensure effective competition" and partly "providing adequate legal security for undertakings".[25]

Technology transfer agreements will in many cases show to improve competition and be pro-effective for a number of reasons. They can reduce the problem of duplicate research and development work, which often can be both time-consuming and costly, thus making future products more expensive to the consumers. Also, such agreements often encourages competition in both the product and technology market, as well as facilitating diffusion.[26] On the other hand, these agreements can also be implemented with less noble results in mind. The licensing of technology with a view to share the market between the parties, for instance, has shown to be a problem. In addition, especially cross-licensing agreements can often work as a barrier of entry to competing products and technology, hindering these access to the market, with the possible results of both less innovation and higher prices for the consumers.

The new TTBE is replacing an old block exemption Regulation on the same field, and introduces new rules. Most visible is the abandoning of the so-called "white-list" in the old Regulation, mentioning certain agreements which normally are permitted, and a "black-list" of prohibited agreements. In the new TTBE, there is only a list of hardcore restrictions that cannot be included in licensing agreements, in addition to a list of "excluded restrictions", which are banned, but which can be removed from the agreement, leaving the rest of the agreement valid.

In order to benefit from the safe harbour laid down in the TTBE art. 2, the agreement in question and the parties must satisfy a number of criteria. Firstly, the agreement must be between no more than two parties, which excludes inter alia so-called pooling of patents. Secondly, the agreement must have as its primary aim the transfer of technology, as defined in art. a (b). This fits well in with the block exemption

[25] Cf. rec. 4.

[26] Cf. rec. 5.

on vertical agreements[27], where art. 2(3) together with paragraphs 30-37 in the Guidelines on vertical restraints[28] exclude inter alia licensing agreements of IPRs from the scope of that Regulation.[29] Thirdly, the market shares of the parties to the agreement must be below certain thresholds, depending on various factors, see art. 3 and chapter 5 of this paper. Further, the agreement must not contain so-called hardcore restraints, as laid down in art. 4 of the TTBE, discussed in chapter 6 of this paper.

However, even if an agreement does not benefit from the TTBE, there is no presumption for illegality under art. 81(1) as such, but will have to undergo a more extensive self-analysis by the parties to the agreement under art. 81(3) EC. This is clearly stated both in the Guidelines and in the recitals to the TTBE.

4.3 The scope of the Regulation

Contrary to other EC-provisions, the TTBE does not include a separate article which defines the scope of the Regulation. In legal terms, art. 1(1)(b) must be read in conjunction with art. 2 first paragraph in order to define the scope. Art. 1(1)(b) is a part of an article concerning definitions, and a 'technology transfer agreement' is defined as a "patent licensing agreement, a know-how licensing agreement, a software copyright licensing agreement or a mixed patent, know-how or software copyright licensing agreement...". In general, this block exemption covers licensing of technology "where the licensor permits the licensee to exploit the licensed technology for the production of goods or services", cf. paragraph 1 of the Guidelines. An agreement can be a simple agreement, a decision of an association of undertakings or a concerted practice, which covers the same forms of cooperation as art. 81 EC, as discussed earlier. Excluded are

4.3.1 Patents, know-how and mixed agreements

The term 'patents' in TTBE does, according to art. 1(h), cover a wide range of registered models; topographies of semiconductors and plant breeder's certificates, to name a few. On a rather more general level, patents are recognisable by two main

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[27] Commission Regulation No 2790/1999 of 22 December 1999 on the application of Article 81 (3) of the Treaty to categories of vertical agreements and concerted practices.

[28] Commission Notice 2000/C 291/01: Guidelines on vertical restraints.

[29] Cf. para 34 of the Guidelines on vertical restraints.

features. Firstly, a patent must be applied for and registered in order to be valid, contrary to for instance copyright, which arise the very same second as a artistic work is created. Patents will also only be valid in the territory it has been registered in, while copyright gives an universal protection. Luckily, the EU has established a "one-stop-shop" for patents, which means that a patent registered, thus satisfying the requirements for registration in one of the member states, will be valid for the entire Community. Secondly, the requirements normally expected for a patent to be valid, are that the patentable subject matter is an invention, that this invention is "susceptible for industrial application", that the invention is new, and that it involves an "inventive step".[30]

Know-how, on the other hand, can be identified by almost the opposite features, cf. TTBE art. 1(i)(I)-(III). Where patents are required to be registered, know-how must not be generally known or easily accessible (the requirement of secrecy), in addition to being unpatentable. In addition, know-how must be substantial and significant for the production, and clearly identified. In art. 1(i) of the TTBE, know-how is dubbed "a package of non-patented practical information, resulting from experience and testing...".

A mixture of patents and know-how seems to be the rule rather than the exception in technology transfer agreements. In many cases, the mere technical drawings, for instance, will not provide the licensee with enough information to apply the technology in question. It can often be helpful for the licensee to obtain access to practical, non-patentable information concerning for instance the production process, or to which traps to avoid.

4.3.2 Computer software

Being probably the most debated topic in IPR-regulation in the EC over the last couple of years, the patentability of computer software is luckily not a topic in the case of TTBE; the Regulation merely include the licensing of computer software in its subject-matter, cf. art. 1(1)(b) on the definition of a technology transfer agreement. This is, however, an important step, since a growing number of industrial processes rely on software in the production of goods, the execution of services or development, especially when such processes are more or less automated. A software licence

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[30] Cf. the European Patent Convention, art. 52.

agreement will then enable the licensee to utilise the same method of production as the licensor, and such a licence may then have the same benefits or downsides to competition as the licensing of patents. Therefore, there are no practical reasons why computer software should be left out of the TTBE. However, as the main protection for computer software today in the EC is still copyright[31], and not patent, there may arise some problems concerning among other things possible modification made by the licensee. Since patents work more or less as recipes, and give the licensor a protection against copying the very *ideas* behind the patented invention, copyright merely give protection against the copying of the *expression*. This is the reason why we for example still have competing operating systems for computers, although they look similar.

Also, as Mario Monti emphasised in his speech prior to the adoption of the new TTBE; "There is no consensus on further broadening the scope to also include copyright in general and trade marks". This is partly due to the fact that, according to Council Regulation 19/65, the Commission has no powers to block exempt anything else than industrial property rights.

4.3.3 The typical licensing agreement - A short overview

When a company or a person obtains a patent certificate (or any other IPR right), there are four ways ahead. One solution is simply to do nothing, thus only enforcing the negative right inherent in an intellectual property right; the right do deny anyone else the benefits of using the knowledge in question. Another way is to decide to solely manufacture the patentable subject-matter, and by doing this, using the positive right of having a monopoly for a time-limited period. A third way can be to assign the patent right, de facto selling the IPR right. The fourth way is to license the knowledge to a third party, finding a middle way between assignment and sole manufacturing. As *Jones and Sufrin* points out[32], licensing must be distinguished from subcontracting, where the aim of the agreement is merely to get a third party to produce a component or carry out a vital process related to the production of the goods in question. In addition,

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[31] See the Software Directive (91/250/EEC) and the Database Directive (96/9/EC). Also, computer software "as such" is for the time being excluded from the subject matter in the European Patent Convention, see art. 52.

[32] Jones & Sufrin, p 575.

subcontracting very rarely fall under art. 81(1), even if know-how is being transferred between the producer and the subcontractor.

Licensing usually involves a licensee obtaining permission from a licensor to produce, sell or incorporate into a product or a process technology which is owned and legally protected by the licensor. There can be many reasons why a company wishes to grant a license, instead of manufacturing the product itself. He may not have the production facilities, storage capacity, access to a distribution network or a geographic location that make it profitable to make the product itself. The licensor may be a recently established company with few assets and weak economic muscles, controlling no property apart from the intellectual ones. On the other end of the scale, some companies have such a size that worldwide sales will be the next step. In such cases, granting a license can be the best way of getting inside foreign markets in other parts of the world, possibly protected by custom rates designed in favour of nationally produced goods. By licensing, the owner of the IPR right in question can also continue the production himself. In addition, licensing can reduce the risks taken by the producer if the product does not hit well with the customers.

Likewise, there are a number of factors which can encourage a company to obtain a license and become a licensee. It will often get the benefit of the experience already gained by the licensor, sometimes both in the manufacturing process and in other fields. Also, it is less expensive than actually buying the company that holds the intellectual property, at the same time that R&D has already been done and paid for. Finally, most licensing agreements are designed in a way that makes the license itself fairly inexpensive, while royalties are paid as the product in fact starts to sell.

However, certain downsides to licensing must be acknowledged. There may be passages in the licensing agreement that prevents the licensee from developing similar product on its own, as well as the life-span of a license have a tendency to be rather long, consistently forcing the licensee to pay royalties and live under a possibly harsh regime of restraints from the licensor. In addition, nobody ever knows how long the licensed product will be a big hit in the market. To live under licensing clauses for years, while the product only sells for a few months, is rarely a good position to be caught in.

What is usually included in and covered by a license, can differ greatly. In terms of the subject matter itself, at least for the purpose of technology transfer agreements, this is determined by the TTBE art. 1(1). In other types of licensing agreements and under other legal regimes, both copyright and trademarks will often be included.

Obviously, a well tailored agreement will state exactly what will be transferred, thus avoiding any misinterpretation on this stage. Secondly, it will be useful to include exactly which obligations the licensor has in the agreement, for instance to what extent he will assist the licensee in technical support, co-operation and enclosure of future improvements. Then, the licensee's obligations must be stated, often in terms of what payments will be made, the level of secrecy and other requirements. In terms of payments, the sum may be a so-called lump sum (a one-time payment), but more often it is being agreed upon a combination of a fee and royalty, a percentage of each unit sold, which can for instance rise if the number of sold units exceeds certain thresholds. Also, it is common to define in which geographical areas the licensee can manufacture and sell the licensed products. This is a field to be careful in terms of avoiding plain market sharing or allocation of customers, and I will get back to this topic under the discussion on the hardcore restrictions in chapter 6.

Guarantees, on both sides may be agreed, although the licensor very rarely will provide a general guarantee on the very results of using the licensed rights. Most frequently, the licensee will provide warranties and public liabilities.

Finally, a licensing agreement should include a passage on termination, either on grounds of possible infringements of the agreed clauses, or in terms of a time-limited period where the licensee shall seize to enjoy the license.

5 Market shares and definitions of the relevant market

5.1 Introduction: The *de minimis* agreements

Anti-competitive behaviour does not automatically mean that a company has overstepped art. 81. If the market shares of the parties to the agreement in question are so low that their behaviour is unlikely to have any impact on the market, the Commission will in most cases not act at all. For instance, if two companies jointly controlling 2% of the product market decide to fix prices, the agreement will only mean that they probably will see their market share decline even further, as their consumers will change supplier when the price undisputedly starts to rise.

These considerations are reflected in the *de minimis*-doctrine, first applied by the ECJ in the case of *Völk v. Vervaecke*[33], which concerned an exclusive distribution agreement for washing machines between the German producer Völk and the Belgian distributor Vervaecke, where Völk only controlled between 0.2 and 0.5% of the relevant product market. Also covering agreements with an 'object' to distort competition, even agreements containing hardcore restraints are exempted.

Based on both case-law and common sense, the Commission's *Notice on agreements of minor importance*[34] was created to inform and guide businesses on where the line should be drawn. However soft-law, the Notice clarifies the de minimis-doctrine on several points, and applies to all of the three different types of agreements in art. 81(1). Firstly, it distinguishes between agreements made between competitors and non-competitors. While competitors fall outside the Notice if their combined market share exceed 10% of the relevant market, non-competitors are allowed a generous threshold of a 15% market share each.[35] Secondly, and most importantly, hardcore restraints in the agreements are not tolerated, namely price fixing, output limitation and market sharing and allocation for competitors, and resale price maintenance and certain bans on active sales for non-competitors.

It is important to underline that the Notice on agreements of minor importance is nothing close to an exhaustive set of rules on this field, but only a way to "...qualif[y], with the help of market share thresholds, what is not an appreciable restriction of competition under Article 81".[36] As the Commission states in paragraph 3 of the Notice, "Agreements may in addition not fall in under Article 81(1) because they are not capable of appreciably affecting trade between member states. This notice does not deal with this issue". Further, the Commission suggests that agreements between small- and medium-sized companies rarely affect trade between member states, suggesting that undertakings employing fewer than 250 people and having less than 40 million Euro as

[33] Case 5/69 [1969] ECR 295, [1969].

[34] 2001/C 368/07, full name "Commission Notice on agreements of minor importance which do not appreciably restrict competition under Article 81 (1) of the Treaty establishing the European Community".

[35] See the Notice paragraph 7 (a) and (b).

[36] See the Notice paragraph 2.

an annual turnover, should as a general rule not be viewed as influential enough to impact inter-state trade.

Also, the so-called NAAT-rule (not appreciably affecting trade), as proposed in a Draft Commission Notice in 2003, suggests a market share cap of 5% of the relevant product market of the very product the agreement concerns, and less than 40 million Euro in turnover a year as a completely safe harbour. As Philip Lowe, the Director General of DG COMP in the Commission stated during a lecture in Barcelona in 2003[37]: "This NAAT-rule is specific to the jurisdictional criterion of effect on trade and distinct from the policy orientations in the Commission Notice on agreements of minor importance, which do not appreciably restrict competition (the —*de minimis* notice“). The latter, in line with its full name, only concerns the question of whether there is no appreciable restriction of competition".

As a result, the NAAT-rule does not, as the de minimis-notice, exclude agreements that contains hardcore restraints. This is underlined in paragraph 50 of the Draft Notice, where it is pointed out that "The NAAT-rule applies to all agreements within the meaning of Article 81(1) irrespective of the nature of the restrictions contained in the agreement, including restrictions that have been identified as hardcore restrictions in Commission block exemption regulations and guidelines". This rule can prove to be important, as a vast number of agreements are being made between firms which have no real market power, and therefore might have been containing themselves in their agreements until now.

5.2 Market share caps in the TTBE, Article 3

As referred to in last chapter, the Draft Regulation released by the Commission in the late fall of 2003 received some harsh criticism on its, as some firms believed, overemphasis on market shares alone. In the final Regulation, it is being distinguished between agreement made between two non-competitors and competing firms. For the latter, the combined market share must according to art. 3(1) not exceed 20% of the relevant market in order to benefit from the block exemption. It is important to keep in

[37] The full text can be obtained at http://europa.eu.int/comm/competition/speeches/text/sp2003_035_en.pdf [October 4th. 2004].

mind that "relevant market" in this context includes both the relevant product market and the relevant technology market.

The fact that the new TTBE focuses on the combined market share of the parties to the agreement, has caused some reactions when a large number of businesses, industry and others (more than 70 in total) submitted their comments already in the spring of 2002. To name one example, the pharmaceutical giant Pfizer complained that the rule of combined market share will have as a result that, de facto, no market leader can ever obtain a safe harbour under the TTBE, no matter how small market share the licensee has.[38] The result being, bear in mind, not an outright prohibition, but a more extensive process, where the company needs to assess the legality of the agreement under art. 81(3). However, it can be pointed out that market leaders, with their size, experience and legal muscles, should be most qualified to make such an evaluation, rather than somewhat smaller sized firms.

Following art. 3(2), non-competitors have the possibility of being slightly more dominant; the safe harbour prevail if neither have a market share over 30% of the relevant market. It will be crucial to note that in art. 3(2), it is each party's market share that is of interest, and not the combined share. As mentioned earlier, the rationale behind this somewhat unequal treatment is the mere fact that cooperation between competitors, who by their very nature are supposed to compete and not cooperate, is viewed as being more harmful to competition than for instance licensing between two firms which operate in completely different sectors. Also, the market share threshold is here the same as in the block exemption for vertical agreements[39], creating a lex specialis on the field of technology transfer, as most non-competitors in these agreements are at a different level of production.

In art. 3(3), the method of calculating the parties' share of the relevant technology market is outlined; the market share is "defined in terms of the presence of the licensed technology on the relevant product market(s)". In other words, the market share for a certain drug held by for instance the licensor and one of ten licensees, when

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[38] Pfizer's comments can, together with many others received by the Commission, be found at http://europa.eu.int/comm/competition/antitrust/technology_transfer_2/ [Valid October 2nd. 2004]

[39] Regulation 2790/1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices.

these are competing, shall be calculated on basis of the market share the licensor and the licensee in question have of the total market.

If the licensing agreement is so successful that the market share of the parties, or on of them, rises above the market share caps, they will continue to enjoy the safe harbour the first year of the agreement, and two more years, as stated in art. 8(2) of the TTBE.

5.3 How to define the relevant market: Main rule and the TTBE-specific provisions

Agreements between companies can be more or less harmful to competition depending on the very nature of the agreement in question, and the restraints inherent in it. However, even the most extreme anti-competitive agreement will never constitute an infringement to the EC competition provisions if the parties to that agreement have no substantial market power.

Defining a company's market share is a two-step process. Firstly, the relevant market must be defined. Secondly, the market share must be calculated. This process is more complicated than it would appear at first glance, especially defining the relevant market in the TTBE, where both the product market and the technology market must be considered. The purpose of this part of the chapter is to explain how the relevant market can be defined when two companies engage in a licensing agreement, and later how the market share of the companies may be calculated.

The general rule on market definition in EC law is reflected in the Commission's Notice on the definition of the relevant market.[40] This text, however soft law, provides a good overview over the Commission's approach to market definition. In paragraph 2 in the Notice, it is pointed out that market definition is a "tool to identify and define the boundaries of competition between firms". In the same paragraph, the Commission emphasise that both the product market and the geographic market must be taken into consideration when defining the relevant product market, however, constrains from potential competition cannot be measured this easily. Following para. 13 of the Notice, both demand substitutability, supply substitutability and potential competition must be

[40] OJ C 372, 09/12/1997.

assessed. In paras. 7 and 8 in the Notice, the relevant product and geographical markets are defined. According to para. 7, the relevant product market "...comprises all those products and/or services which are regarded as interchangeable or substitutable by the consumer, by reason of the products' characteristics, their prices and their intended use". The geographic counterpart is defined in para. 8, as comprising "...the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different in those areas".

In this chapter, I will start by explaining the idea of market power, the general methods of measuring the relevant product and geographical markets, and then show the specific market definition and considerations included in the TTBE.

5.3.1 Market power

Central in the determination of market power is the economic term of demand elasticity. In short, this concerns whether or not a company can raise the prices for its products or services without losing sales. This is determined by a number of factors, for instance, the company's market share in the relevant market, the number of competitors in that market and the number and level of barriers to entry and exit.

Having market power, however tempting it may sound, is believed to be the greatest threat to competition. Companies which have obtained market power, and exercising it, create a unhealthy competition environment and can be responsible for raised prices for the consumers. In dominance cases, the *exercise* of that power is the greatest concern, since having dominance is not a sin in itself. However, in the ECMR, the mere possibility of a company *gaining* market power by merging can be enough for the Commission to stop a concentration. And in cases concerning horizontal or vertical agreements between companies in art. 81, it is the gaining of market power through agreements which is the main topic. Here, too, it is the *possibility* of two companies gaining too much market power by cooperation that is enough to deem the agreement prohibited after art. 81(1) and void after art. 81(2).

5.3.2 Barriers to entry and exit

Being part of the big picture of market power, barriers to entry and exit can easily be forgotten, though this is the very core of the topic. If a company has a dominant share of the market, this can be lost even before it can abuse its dominance or engage in agreements with hardcore restraints, if there are no barriers to entry en exit.

This can be illustrated by what has happened on the software market the last 20 years. In 1984, Apple had almost monopoly in home-computer software. In 1995, nearly 100% of all internet browsers in the world were produced by Netscape. Today, Microsoft has a monopoly in both sectors. This can happen because the barriers of entry and exit have been historically low in this industry. The transportation cost of the product is almost zero, national legislating has mostly been harmonised and the production itself requires no factories - in theory only a CD-writer. The cost of establishing a software company is low; all that is needed is really an office and a computer. To penetrate foreign markets, licensing can be used. Then, if the plans do not work out, sunk costs are rarely high. Computer software is protected by copyright and generally not patents, which means that "stealing" ideas from others, as Microsoft did in both the examples above, is allowed, as long as the "expression" is not copied.

According to *Whish*, the Oxford dictionary defines barriers to entry as "laws, institutions, or practices which make it difficult or impossible for new firms to enter some markets...".[41] A better legal definition has been put forward by Jones and Sufrin, where Stigler from the so-called Chicago-school defines barriers of entry as "...a cost of producing (at some or every rate of output) which must be borne by a firm which seeks to enter the industry but is not borne by firms already in the industry".[42] The first definition does for instance not distinguish between cases where it is hard to gain access (high sunk start-up costs, many competitors, high degree of anti-competitive agreements between existing firms) and cases where it is impossible to get into the market, for instance due to IPR-rights which confers a legal monopoly.

Another topic for debate has been whether the barriers of entry are only barriers for new firms at this point in time, or if it also includes barriers that any firm had to battle at some point, as for instance the costs used on advertisement to establish the firm

[41] Whish 2003 p 44.

[42] Jones & Sufrin p 53.

in the market. In the EU, the Commission has adopted a wide definition, as shown for instance in numerous cases under art. 82.

5.3.3 The relevant product market

For many firms, the result of a definition of the product market can prove to be rather surprising. With an extremely narrow definition, almost any producer can be said to not only overstep the thresholds of the TTBE, but almost end up as a monopolist. This can be illustrated again by the cases of *Continental Can* and *United Brands*, although these were dominance-cases under art. 82. In *Continental Can*, the Commission found that metal cans for fish, meat and metal tops belonged to different product markets, thus choosing a very narrow product market definition. However, the Commission failed to justify its interpretation to the ECJ on appeal. In *United Brands*, the ECJ laid down the legal test of interchargability; The question whether bananas were part of the fruit market or the banana market boiled down to whether bananas had "special features distinguishing [them] from other fruit that [are] only to a limited extent interchangeable with them". In this example, the difference between the market share of the narrow market and a wider market can be rather big. In effect, a well proved wide definition of the relevant product market delivered by the company can save it from both monopoly proceedings and from exceeding market share thresholds in block exemptions.

If products are interchangeable, they belong as a main rule to the same product market. Interchargability is, as mentioned in the Notice on the relevant market, based on the idea that products can be divided into groups of similar products if they "share the same characteristics" (*Continental Can*) or are "singled out by such special features..." (*United Brands*).

When two products are found to be interchangeable, they belong to the same product market, thus the borders of the product market are expanded to comprise two products rather than one. To illustrate this, we can imagine a company producing pens with blue ink, which has a market share of 40% in the market for blue pens. If blue pens are found to be interchangeable with for instance pens with black ink, and another company has a market share of 40% in that part of the market, the two companies will each have a market share of only 20% of the total market (provided that the sales value of blue and black pens were roughly the same). In this example, the companies moved from dominance after art. 82 to within the borders of most EC block exemptions, including the TTBE's market share cap for competing firms, simply because the market definition widened the relevant product market.

5.3.3.1 Demand-side substitutability

In order to measure interchargability, reliable data must be collected, and a common market definition must be found. The introduction of both the self-assessment regime, the new block exemptions and the new European Community Merger Regulation (ECMR), which all focuses on market shares, has indirectly made this process more important than ever before.

The main part of this measurement is that of demand-side substitutability. The core of this is explained in the Notice paras. 15-17, where this assessment "entails a determination of the range of products which are viewed as substitutes by the consumers". Vital in this context is then not only the characteristics of the products themselves, but also whether the consumers can switch between them. For the purpose of determining this, the so-called "SSNIP-test" has been developed. This test, first invented and applied in the USA, is based on a situation where the product in question has a hypothetical price-rise; a Small but Significant Non-transitory Increase in Price (SSNIP). The question will thereafter be whether the consumers would switch to a similar and less expensive product. If they do so, the product market must be wider and comprise more than only the first product. The level of the increase in price is generally believed to be in the range of 5-10% of the retail price, this is also suggested in para. 17 of the Notice.

The SSNIP-test does also apply in the measuring of the relevant technology market in the TTBE, cf. para. 22 of the Guidelines to the TTBE. Here, the question will be whether the licensee will switch to other technologies if the price (for instance the initial sum or the royalties) is increased.

However, the SSNIP-test must be applied with caution. Also dubbed "the hypothetical monopoly test", the test will generate plain wrong results if the product in question is already priced superficially high. This effect, often referred to as "the Cellophane Phallacy"[43], or "own price elasticity", occurs when consumers are presently at a point where they are ready to completely discontinue the purchase of the product, due to an already superficially high price, something that can easily happen in a monopoly-like situation. Although they stop buying product A in this situation, they will not necessarily switch to product B, but choose to live without the product, or replace it with something they would not normally choose. In the Du Pont-case, the monopolist company argued that the market for cellophane was part of a bigger market for packaging materials in general. By applying the SSNIP-test, Du Pont could not raise the price without losing customers. However, this was not due to effective competition, but rather that this cross-elasticity, where consumers switch between products, took place because the price was already too high. Had it been at a normal, competitive level, the consumers would not have switched to the other products.[44] To make a rather extreme example; if the price of meat was at a monopoly-like level, then raised by 10%, and customers chose to buy yellow turnips and pretend this was meat, would not mean that meat belonged to the same market as yellow turnips.

Applying the SSNIP-test will therefore, in certain cases, make us believe that the relevant product market is wider than it really is.

5.3.3.2 Supply-side substitutability

Though less important than demand-side substitutability, supply-side substitutability must nevertheless be taken into consideration in a market analysis. The main question in this relation is, judging from para. 20 in the Notice, whether suppliers (other than the current ones) can switch production to the product in question in response to the same small, but permanent increase in price. In many cases, supply-side substitutability is simply a question of "quasi-potential" competition; if it becomes more profitable, can other suppliers start the manufacture of the product "without incurring

[43] After the Du Pont-case, which concerned domination in the cellophane market.

[44] See further on the whole topic Bishop & Walker p 49 and Jones & Sufrin p 46-48.

significant additional costs or risks"?[45] The most common example[46], is the one on paper production. Shifting production from a cheap to a slightly more expensive paper quality can be done without major changes. In such cases, the products belong to the same product market.

As Whish points out[47], where cases are more complex than the paper-example, it is really a question of market power, rather than one of market definition, as applied in US antitrust practice. Market power determination comes at a later stage in the process, and does undoubtedly contain market share-related consideration. However, even if a company has a market share of 100 %, it will never be viewed as for instance dominant, if the potential competition is high and the barriers of entry and exit are at a minimum. But a company like that will never benefit from the safe harbour in the TTBE, since one of the main qualifications here is based on market shares, and not market power.

5.3.4 The relevant geographical market

At first glance, art. 3 of the TTBE does not seem to care about the relevant geographical market. However, in para. 20 of the Guidelines, it is explained that the term "product market" refers to goods and service markets "in both their geographic and product dimension".

The geographical market can be rather difficult to assess, simply because the EU is intended to be a single market where goods and services shall move freely across the borders. It would then seem as the Community itself is always the relevant market, if not a part of a world market for some products. But national markets still exist within the Union, as shown for instance in the TV-listings-case[48], where the relevant geographical market was Ireland and Northern Ireland, since the TV-channels in question primarily where offered in this particular area. In the Volvo/Scania merger decision, the Commission denied the merger partly because it found that it existed a

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[45] Cf. the Notice para 20.

[46] See for instance the Notice para 22.

[47] Whish 2003, p 32-33.

[48] Case T-69/89 etc RTE v Commission [1991] ECR II-485, [1991] 4 CMLR 586.

national, Swedish market for trucks and buses, and that this market was separate from the European market.

Quite often, the products or services themselves determine to what extent the market can be Union-wide. Milk, for instance, have a short life-span, while computer programs can easily be distributed worldwide. Sometimes, but rarely because of art. 28 and the single market imperative, national laws in some member states set limits to the geographical market. Swedish "snus" is for instance banned in the rest of the Union. Language barriers play in as well; a Dutch television program or a book will probably not be a part of a Union-wide market, unless translated. Other factors can also play in, as for example transportation costs and different taste and habits throughout the Community.

Also on the field of geographic market analysis, the SSNIP-test can be applied. If consumers switch to foreign producers if the price of a certain product rises nationally, the market must be geographically more widely defined. This is well illustrated by both parallel imports and the strange phenomenon of Europeans crossing borders to shop typically tax-sensitive goods as alcohol and tobacco in other member states which impose lower taxes on these goods. In such cases, the market is certainly wider than each member state only.

Demand fluctuations are also of importance, constructing a "temporal market" in certain cases. This mostly applies to season-sensitive goods and services, as for instance fruits, organised holidays to Greek islands or wrapping-paper for Christmas gifts. In *United Brands*, bananas where found to be less popular in summer, when other fruits could be bought cheaply, thus suggesting no market power in that particular season. This was, however, not dealt with by the ECJ, and the Commission refused to acknowledge such a temporal market in this case.

5.3.5 TTBE: The relevant product *and* technology market

If two companies are trying to get a safe harbour for their licensing agreement under the rules of the TTBE, however, not only the product market, but also the technology market is of importance. As mentioned in paragraph 20 of the Guidelines to the TTBE, technology is an input integrated in a product or a production process. Therefore, licensing agreements can affect the competition in the product market for goods and services as well as in the market for similar technologies. To name an example, if the companies A and B enter an agreement concerning the licensing of a software codex for compressing music files, where company A is engaged solely in computer technology whereas company B only produces a certain device for playback of music, the agreement does not only affect the market for such devices, but also the market of competing technologies for music compression, and possibly also other markets.

As a general rule in EC competition law, the relevant market must be defined first. In the field of technology transfer, the parties to an agreement can be either competitors or non-competitors, with a respective market share cap of 20% and 30%. The distinction between competitors and non-competitors needs an explanation. As a main rule, the parties to an agreement are competitors on the relevant product market if they are actual or potential suppliers of competing products. On the technology market, however, they will only be competitors by means of actual competition; in other words if the parties license technology that compete (as substitutes in the same relevant product market). Therefore, as a combination of product and technology markets, they will only have the relief of being non-competitors after the TTBE if the *licensor* is neither an actual nor a potential supplier of the products and the *licensee* is currently not licensing a competing technology.[49] This distinction will be important not only in terms of market shares, but also in connection to the banned hardcore restraints, which differ somewhat between competitors and non-competitors.

As Monti has explained[50], the licensee does not become a competitor of the licensor simply by producing under the license. The problem is, however, that the two parties can become competitors during the life-span of the agreement for other reasons, for instance if the licensee develops its own, competing technology, and then start to produce and possibly license this technology to third-parties. This is inter alia reflected in art. 4(3) of the TTBE, where the hardcore restraints that applied to non-competitors shall continue to apply for the rest of the life-span of the agreement, even though the parties become competitors, provided that the agreement is not "subsequently amended in any material respect".[51] In paragraph 31 of the Guidelines, the Commission states that

[49] Cf. art. 1 (j) (i-ii) of the TTBE.

[50] Monti's speech, page 4, 4th. para.

[51] Cf. art. 4 (3).

it will "mainly focus on the impact of the agreement on the licensee's ability to exploit his own (competing) technology", which is the view that has been materialised in art. 4(3). Also, if the licensor enters the product market where the licensee already has been active *after* the agreement was concluded, the hardcore list for non-competitors will still apply.[52]

After the relevant market has been assessed, the market share must be calculated, or as it is put in the Guidelines, para. 23; "Once relevant markets have been defined, market shares can be assigned to the various sources of competition in the market and used as an indication of the relative strength of market players". As laid down in art. 8 of the TTBE, it is the market sales value data that as a general rule will be the basis for this calculation, and not the mere units sold. However, art. 8(1) second paragraph suggests that in some circumstances, when sales value data are unavailable, other sources must be used. The solution is to use "other reliable market information"[53], where sales volumes is pointed out as the main source. This rule does not seem to be exhaustive, suggesting that also other types of market information can be used. Following art. 8(1) third paragraph, the data used shall relate to "the preceding calendar year".

One method to calculate a technology's market share is put forward in the Guidelines paragraph 23; the market share of each type of technology can be calculated on the basis of the total income from royalties gained from licensing of that particular technology, since one would not think sales value can be used when measuring the income from technology only. However, as pointed out in the Guidelines, this method is rather theoretical, and the size of the royalties can be more or less secret. Therefore, the solution used in art. 3(3) of the TTBE, is in fact to calculate on the basis of the sales value of all products *incorporating* the technology in question, even competing technologies that are not being licensed, which is the same approach chosen in paragraph 70. This way, potential competition can also be measured, as other firms on the relevant product market, which can easily start licensing their own technology if the price of licenses increase, will be included as well. And equally important: a high income from licenses does not necessarily mean that the company has market power. In

[52] Cf. para. 31 i.f.

[53] Cf. art. 8 (1) 2nd. para.

addition, this excludes technology which is only used in-house, cf. art. 3(3) of the TTBE.

6 Hardcore restraints

6.1 Introduction

As stated in rec. 5 to the TTBE, licensing agreements are usually not regarded to be among the most anti-competitive agreements in the eyes of the Commission. On the contrary, they "will usually improve economic efficiency and be pro-competitive"[54]. However, to benefit from this block exemption, the group of agreements in question must "be assumed with sufficient certainty" to fall under the exemption in art. 81(3), cf. rec. 9. And, both in line with the jurisprudence of the ECJ and earlier block exemptions, there are a number of agreement clauses which typically can be viewed as being severely anti-competitive, and which at the same time cannot be said to be "indispensable to the improvement of production or distribution", cf. rec. 13. And even agreements clauses which fall under the TTBE in the first place, can have their safe harbours withdrawn by the Commission at any given time, provided that the effects of the agreement shows to be anti-competitive, cf. art. 6 of the TTBE and rec. 16.

Nevertheless, as we shall witness in this chapter, will a hardcore restraint indeed not be a fixed term. As explained in para. 74 of the Guidelines, the definition of a restriction as hardcore is "based on the nature of the restriction and experience showing that such restrictions are almost always anti-competitive". Further, both the objective of the agreement clause in question and circumstances in the individual case will play in.

In the TTBE, different levels of severity are assigned to respectively agreements between competitors and agreements between non-competitors, the latter type of agreements having much resemblance with vertical agreements, which has been given their own, quite generous block exemption. This different treatment is noticeable in mainly two ways. Firstly, as mentioned in chapter 4 and 5, the market share caps are

[54] Cf. rec. 5.

different. Secondly, and closely linked to the main topic in this chapter, the hardcore restraints are defined differently.

In the case of technology transfer, not only the product market is crucial in order to distinguish between competitors and non-competitors, but also the technology market. The result is that if two companies are not competitors in the product market, but still utilise the same technology, they will be treated as competitors.

Contrary to the so-called excluded restrictions will there be no severability for hardcore restraints, in other words; the problematic clause can not be "cut out of" the agreement, while the rest of the agreement is block exempted. The result is therefore that the agreement as a whole falls outside the block exemption if it contains a hardcore restriction, cf. the Guidelines para. 75. With this in mind, the main critisism the Commission received after publishing its draft of the TTBE in October 2003, was that the hardcore list was "over-inclusive"[55], and therefore probably would not facilitate licensing the way it was intended to. This was particulary visible in terms of licensing between competitors, where for instance non-reciprocal licensing between competitors now is treated less dogmatic. Also, the hardcore list in the draft Regulation included all passive and active sales bans in agreements between competitors, however non-reciprocal the agreement might be, a feature which is also changed in the final text.

To explore the limits of the hardcore restraints, it will be necessary to draw lines to general interpretation of art. 81(3), as shown in the Guidelines. This will be done when appropriate throughout this chapter.

Finally, as repeatedly stated by the Commission; even a hardcore restriction can in theory be exempted under art. 81(3), since no agreements are excluded from this article *per se*, even if such a result would be highly unlikely and has shown to be extremely rare in the history of the EC competition regime.

6.2 Agreements between competitors

The hardcore restrictions in agreements between competitors are placed within the very core of the TTBE, since such agreements are those which possibly can pose the greatest risk to competition. In agreements between competitors, there is a distinction

[55] See World Competition Law and Economics review, vol. 27, No. 3 p 351

between so-called reciprocal and non-reciprocal agreements, where the first are agreements containing cross-licensing of technology, if such cross licensing concerns *competing* technologies that can be used in the production of *competing* products. Therefore, if competing technology used for producing non-competing products are being cross-licensed, the licensing agreement will be a non-reciprocal one. If only one party license technology, the agreement will be non-reciprocal as well, cf. para. 78 of the Guidelines. The mere licensing of improvement from one of the parties, or a grant-back obligation, does not make the agreement reciprocal. However, if either the licensor or the licensee at a later stage agree on a second license between the same parties, especially if this is done shortly after the first license, the agreement will become reciprocal. This distinction will prove to be important, as the rules in art. 4 are generally stricter for reciprocal agreements, as these can be used to set up a cartel or other market allocation arrangements.

In the field of licensing between competitors, there are five types of clauses which can be said to be hardcore restraints. As stated in art. 4(1), price fixing, limitation of output, market- or consumer-sharing (allocation of markets and consumers) and restrictions placed upon the licensee hindering him to exploit his own technology are hardcore restraints. In addition, restrictions as to what extent the parties can carry out research and development (R&D) is also defined as a hardcore restriction in art. 4(1), but only in cases where such a restriction is not indispensable to prevent licensed know-how from being disclosed to others.

However, this hardcore list cannot be applied without certain exemptions. These will also be acknowledged and explained over the following pages, where each of the groups of hardcore restrictions between competitors will be examined.

6.2.1 Price fixing

Price fixing between competing companies has always been regarded as one of the most anti-competitive measures firms can engage in under EC competition policy, and the practice is listed first under the prohibition rule in art. 81(1). The effect of this cartel-like behaviour is almost always increased prices for the consumers, and usually, this is also the very *object* of such an agreement clause. Price fixing agreements are also extremely unlikely to produce the wanted effects and fulfil the four criteria listed in art.

81(3), as they inter alia almost never are indispensable to the object of "[...] allowing consumers a fair share of the resulting benefit", since the aim usually is the opposite. One of the few exceptions can be found in *Uniform Eurocheques*[56], where the commission fee for cashing in Eurocheques was fixed. Here, the Commission granted an individual exemption since it found that the agreement in this case was for the benefit of the consumers, who would know the common amount of money they were charged. The same happened in *Visa International*[57], only this time the subject matter was the intercharge fee between issuing and acquiring banks in the Visa-system. A somewhat less logical decision was made in AuA/LH, where an agreement containing both price fixing and market sharing between the two airline companies Austrian Airlines and Lufthansa was individually exempted, mostly due to the "important synergistic effects" such an agreement was found to have[58]. The fact that the exemption came at a time when airliners throughout Europe were struggling to avoid bankruptcy did probably play in. Nevertheless, the Commission found this agreement to enhance the overall service level offered to the consumers.

The rule in art. 4(1) held together with art. 4(1)(a) of the TTBE gives a non-application of the benefit of the block exemption to agreements which "directly or indirectly, in isolation or in combination with other factors under the control of the parties, have as their object" ... "the restriction of a party's ability to determine its prices when selling products to third parties". In technology transfer agreements, this can have the form of a direct agreement on the level of prices charged, possibly with agreed maximum rebates, cf. the Guidelines para. 79. Secondly, a more indirect way of fixing prices can be infringing art. 4 (1) (a) where the parties agree on "disincentives"[59] to set a different price than the recommended one, for instance by raising the rate of the royalties if the products are sold at a rebate price. As emphasised in the Guidelines para. 79, the mere obligation on the hands of the licensee to pay a minimum royalty is not caught by the prohibition.

Thirdly, where royalties are calculated on basis of the total number of products sold by the licensee, even those which do not incorporate the licensed technology, art.

[56] OJ [1985] L 35/43 [1985] 3 CMLR 434.

[57] OJ [2002] L 318/17, [2003] 4 CMLR 283.

[58] A parallel may be found in the exemptions made for certain liner conferences by the Commission.

[59] Cf. the Guidelines para 79.

4(1)(a) will be infringed. In these cases, the agreement will restrict the licensee's ability to use his own technology, which also is caught by another hardcore prohibition, namely art. 4(1)(d). However, this sort of agreements can in certain cases fulfil the conditions laid down in art. 81(3), but only where it will prove difficult to calculate the amount of royalties payable by the licensee since the "licensed technology leaves no visible trace on the final product"[60], and alternative methods to calculated the royalties are absent.

Finally, in cases where the parties calculate the royalties on the basis of individual sales, the royalty level impacts on the marginal cost of the products. This *can* be used as an excuse to fix prices, and is often seen in cases where the parties use cross-licensing combined with running royalties. The case of so-called running royalties in licensing agreements have been a topic for debate in the time before the adoption of the new TTBE. As Monti points out[61], such clauses usually are agreed upon in order to share the risk between the licensor and the licensee, as royalties are calculated on the basis of individual sales. However, running royalties can also be used to set up a disguised cartel, especially in combination with cross-licensing, which was viewed as hardcore in the draft Regulation - and widely critisised. The result in the final text is that such agreements only fall under the hardcore definition if the license agreement in question is proven to be a hidden cartel, while running royalties as such is not defined as being a hardcore restraint. The parties must therefore have a legitimate, pro-competitive purpose with such agreements.[62] *Dolmans* underlines[63] that it is a common practice to calculate on the basis of individual sales, and that this practice in no way sould be seen as collusive behaviour *per se*.

6.2.2 Limitation of output

A restriction on the level of output is defined in the Guidelines to the TTBE as "a limitation on how much a party may produce and sell"[64], and in terms of technology

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[60] Cf. the Guidelines para 81.

[61] Monti's speech, page 5.

[62] See further Monti's speech page 5 and the Guidelines para 80.

[63] See World Competition Law and Economics Review p 356.

[64] The Guidelines para 82.

transfer agreements, it can be a limitation on the amount of products sold both by the licensor and the licensee. Many of the hardcore restraints in art. 4 seem to be concentrated around the thought that the licensor lays down restrictions on the licensee, but in many cases, it will be important to keep in mind that the licensee can the strong party as well. The prohibition is found in art. 4(1)(b), and does not cover cases where the licensee gets his output of contract products limited in a non-reciprocal agreement, or on only one of the licensees in a reciprocal agreement. This is one prime example of how non-reciprocal licensing agreements are treated less hard than reciprocal ones.

Art. 81(1) specifically prohibits agreements with a view to "limit or control production, markets, technical development, or investment", at the same time as such agreements are unlikely to benefit from art. 81(3), since they rarely are "indispensable". The exception is believed to be certain specialisation agreements. It is a known fact that limited output can contribute to higher prices by distorting the balance between supply and demand, the best example is probably OPEC, the cartel consisting of a number of oil producing countries who collude in limiting the output each time the oil price gets too low. The Commission has on a number of occasions been striking down on all sorts of output limitations as well as more advanced quota-arrangements, often in conjunction with market sharing or price fixing. Most serious, of course, are situations where a number of companies controlling a majority of the market engage in output limitation, as are situations where the licensor use a standard licensing agreement where a number of licensees are obliged to participate in the same cartel-like behaviour. The *Quinine Cartel*[65] was the first time the Commission fined firms for output limitation, and freezing of market shares in the form of output limitation was condemned by the Commission in *Cartonboard*[66].

Art. 4(1)(b) only targets reciprocal output restrictions on both of the parties to an agreement output restrictions on the licensor. The reason why other, non-reciprocal agreements containing output limitation is exempted, is according to the Guidelines para. 83 that one-way restrictions inter alia "not necessarily lead to a lower output on the market". As for reciprocal agreements where only one of the licensees must agree on output limitation, this may be a result of the technology cross-licensed by that licensee simply is of higher value than the technology of the other licensees. Therefore, this is

[65] OJ [1984] L 220/27, [1985] 2 CMLR 108.

[66] OJ [1994] L 134/1, [1994] 5 CMLR 547.

believed by the Commission to promote further improvements of technology as well as increased technology competition and R&D, since the other licensees may struggle to develop better technology. These considerations are mentioned in the Guidelines para. 83.

6.2.3 Allocation of markets or consumers

The allocation of markets and consumers is directly contrary to the single market imperative, which is one of the core purposes of the EC, as it is highly likely to hinder intra-brand competition and the free movement of goods and services between member states. The result is often, as mentioned, higher prices and in some cases a reduced availability in certain areas. As Whish points out[67], market sharing can be more "effective" for the typical cartels than price fixing, since it removes the price competition completely, and is an easier agreement to implement. Agreements implementing market sharing of various degrees of severity is, both in terms of agreements between competitors and non-competitors, especially widespread in technology transfer agreements, where it is also exempted from the hardcore list in the TTBE in a variety of cases. However, as a main rule, market sharing is mentioned as a particularly anti-competitive measure, having competition distortion as its very object, in art. 81(1)(b). It is also considered to be a hardcore restraint in all EC block exemptions.

The Commission has identified market sharing in a number of cases, one of the most grave probably being *Pre-insulated pipes*, where the whole EU-market was divided, and the participants were fined 92 million euros.[68] Also, a "home-market"-practice has been struck down upon, inter alia in *Cement*[69], where the participants had agreed not to export cement into other territories. Because of the important single-market imperative, market sharing agreements are unlikely to benefit from art. 81(3), even though it has been found to be indispensable in a few cases.[70]

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[67] Whish 2003 p 477.

[68] OJ [1999] L 24/1, [1999] 4 CMLR 402, upheld in Cases T-9 etc HFB Holding v Commission [2002] ECR II-1487, [2001] 4 CMLR 1066.

[69] OJ [1994] L 343/1 [1995] 4 CMLR 327.

[70] See for instance *Transocean Marine Paint Association*, JO [1967] L 163/10, [1967] CMLR D9.

In art. 4(1)(c), the prohibition concerns "the allocation of markets or customers", while the provision entails a "white list within", containing a number of allowed types of agreements. The main prohibition concerns competitors in a reciprocal agreement, agreeing not to produce or sell in certain areas, including a ban on active and/or passive sales into other territories, as well as to certain customers. When the agreement is non-reciprocal, a number of exemptions are listed in art. 4(1)(c)(i-vii).

6.2.3.1 Exceptions from the hardcore list in cases similar to market sharing in non-reciprocal agreements

As non-reciprocal agreements are less likely to distort competition, these enjoy certain exceptions to the prohibition on agreements containing elements of market can customer sharing, cf. art. 4(1)(c)(ii), (iv-v) and (vii). The rationale behind these somewhat generous exceptions, allowing i.e. restrictions on both active and passive sales, is explained by Monti as a way to "provide sufficient protection to the licensor in order to encourage him to license his technology".[71] These exceptions were narrower in the old TTBE, and the general idea seems to be that the licensor would be less likely to engage in technology transfer agreements if he did not get the ability to protect himself by these measures. Further, the licensee will probably be encouraged to enter an agreement if he gets an exclusive licence.

In (ii), exclusive licenses are exempted, both when a limitation is set on the technical field of use and product markets. Quite often, a licensee is granted a certain territory where he is protected from competition from other licensees as well as the licensor himself. The reason why this is allowed, is simply because the licensee should be given a chance access the market and invest in the technology. As the Guidelines para. 86 states, the object of these agreements are "not necessarily to share markets".

As in (ii), point (iv) block exempts non-reciprocal agreements where the licensor and the licensee agree not to engage in active *or* passive sales into the exclusive territory of the other party, cf. point (ii). The rationale is the same as in (ii); a shared interest between the licensor and the licensee to protect investments, while the risk of hardcore market sharing as the very object of the agreement is less likely.

[71] See Monti's speech, page 5.

In point (v), restrictions on active sales by the licensee into territories reserved for other licensees by the licensor, both by means of customers and markets, and where the latter is not a competitor of the licensor, are block exempted. The reason for this exception is to create an equity of arms between the licensee who is competing with the licensor, and the non-competing licensee who is protected in these agreements, who is not on the market. Here it is important to remember what a technology transfer agreement is all about, as agreements between licensees do not involve any transfer of technology and are thus not covered by the TTBE, nor are agreements between more than two parties. These latter mentioned agreements can amount to cartel activity, and are not certainly not block exempted, cf. the Guidelines para. 89.

Point (vii) excepts cases where the licensee is obliged to engage in "backup-production", or an alternative source of supply for one customer only, no matter how many licenses concerning this customer have already been given by the licensor. The main reason why this way of customer-allocation is allowed, is because it is highly unlikely to have a grave impact on competition.

6.2.3.2 Field of use and captive use restrictions

A field of use restriction is exempted from the prohibition in art. 4(1)(c) in art. 4 (1)(c)(i), while captive use restrictions are exempted in art. 4(1)(c)(vi).

A field of use restriction limits the parties' ability to use the licensed technology to produce other products or implement it in other technical processes than those agreed. This exceptions from the hardcore main rule is valid regardless of whether the agreement is reciprocal or non-reciprocal, however, this was not the initial proposal of the Commission, as it suggested that only field of use restrictions in non-reciprocal agreements should be block exempted. The firms and institutions submitting comments on the proposal argued fiercely against this division, subsequently managing to alter what was to become the final TTBE. As Monti explains, the risk of hidden market sharing in reciprocal agreements are indeed higher, but "less prominent in case of field of use restrictions than with reciprocal territorial or customer restrictions, as it is less likely that competitors withdraw completely from a particular product market".[72] For the block exemption to be valid, however, the Commission have laid down two

[72] See Monti's speech, page 5.

conditions in para. 90 of the Guidelines; the restrictions must not concern anything else but the licensed technologies, and the parties must not be limited in the use of their own technologies, cf. the prohibition in art. 4(1)(d).

Captive use restrictions are defined in the Guidelines para. 92 as "a requirement whereby the licensee may produce the products incorporating the licensed technology only for his own use". These restrictions are exempted from the hardcore list in art. 4 (1)(c) (vi), as they can be a good way to spread the technology in question between competitors. Most common are clauses where the licensee agree not to sell components to other producers, however, an obligation on the licensee not to sell spare parts for his own products, will not be exempted, cf. (vi) and para. 92 of the Guidelines.

6.2.3.3 Sole licenses

In art. 4 (1)(c)(iii), sole license agreements are not defined as hardcore restraints. As mentioned[73], a sole license gives the licensee a somewhat limited exclusivity in the way that no other licences will be given in the same territory, contrary to more hardcore exclusivity licences, which will give near total exclusivity. A sole license does in addition often not exclude the licensor from the market in question. Here, the rationale behind the exception is that sole licences are of such a limited competition distorting nature that they are exempted even in reciprocal agreements. In addition, and as explained in the Guidelines para. 88, such agreements do not hinder the parties in using their own technology in the other territories.

6.2.4 Restriction of the use of a party's own competing technology

This particular hardcore restraint is more serious that it may appear at first glance, as it has the potential to restrict both intra- and inter-brand and -technology competition, in addition to in effect keeping the licensee away from improving his own technology. In art. 4(1)(d) first alternative, such restraints are defined as hardcore. According to the Guidelines para. 95, the main issue with restrictions on the licensee's

[73] See the Nungesser-case in chapter 4.

ability to use his own technology, is the fact that such a clause make his technology less competitive than the licensed technology. The hardcore restriction also covers both agreements where the licensee is obliged to pay royalties on products incorporating his own technology, as well as a ban on the licensee on licensing out his technology.

6.2.5 R&D-restrictions

Restrictions in the parties' abilities to engage in or carry out research and development (R&D) can have a slight chance of restricting competition, but first of all, it can delay improvements and innovation in the field of the licensed technology. Therefore, art. 4(1)(d) second alternative defines as a main rule such restrictions as hardcore, while the Guidelines uses basically the same arguments as mentioned in 6.2.4. Such restrictions imposed on the licensee in terms of possible R&D-agreements concerning his own technology is also covered.

However, if such a restriction is indispensable to prevent third parties from getting to know the secret know-how inherit in a technology transfer agreement, it shall be exempted from the hardcore rule. Indeed, one of the main characteristics of know-how is that it is secret. Such a disclosure would then ruin parts of the licensed subject-matter, creating a loss for the licensor.

6.3 Agreements between non-competitors

TT-agreements between non-competitors are block exempted when neither of the parties have a market share exceeding 30% of the relevant product and technology market, cf. art. 3(2). Here, slightly different considerations form the basis for the hardcore restraints banned in art. 4(2). While anti-competitive agreements between competitors can have a direct impact on the intra-technology competition, agreements between non-competitors can have an equally grave impact on the inter-technology competition. In some cases, blocking positions, either one-way or two-way, exists, meaning that the licensed technology cannot be used without infringing a second technology. In these cases, the parties are considered to be non-competitors, which they in general view as positive, due to both the market share cap and the somewhat different hardcore list. The legal problem here is the Commission's emphasis on "objective" factors to prove such a blocking position, cf. para. 32 of the Guidelines. This may prove to be costly for the firms involved, since their own in-house assessment would hardly be deemed objective.

6.3.1 Price fixing

In art. 4(2)(a), restricting a party's ability to determine its prices when selling to third parties is defined as a hardcore restraint. The practice targeted here is usually different ways of achieving minimum pricing, and not suggested maximum prices or recommended prices, since the latter would less likely make the products in question more expensive. Also included are more indirect ways of fixing the retail price, as listed in the Guidelines para. 97, and which can be anything from setting up a price monitoring system in order to identify cases where the other party is cutting prices, to more grave behaviour as outright threats and intimidations from one party, forcing the other party to raise prices. Most common, however, are agreements implementing a whole spectrum of different financial incentives to make the licensee coordinate selling prices with either the licensor or with other licensees. As mentioned in the Guidelines para. 97, quantity-rebates in the form of most-favoured-customer(s) may be one of the most common.

As mentioned under agreements between competitors; price fixing is a serious threat to competition, and will in most cases lead to higher prices for the consumers. Being a hardcore restraint, it must satisfy the conditions of art. 81(3) EC in order to be legal outside the safe harbour of the TTBE. This is usually not an easy task for such restrictions, as it rarely transfer any part of the gain to the customers.

6.3.2 Restrictions of the licensee's active and passive sales

Agreements forcing the licensee to restrict his passive sales of products incorporating the licensed technology are defined as hardcore by art. 4(2)(b), and is in many ways the equivalent to market sharing under art. 4(1)(c). Judging from both the prohibition itself and the Guidelines, both direct and indirect measures are targeted. One way of actively restricting passive sales may be obligations to not sell to certain customers, or customers in specific territories, as well as being forced to refer orders from customers outside the licensee's territory to the respective other licensees. A wide range of indirect ways of achieving the same goal are mentioned in the Guidelines para. 98, i.e. a verification system set up to monitor which of the licensees are selling the goods at a price regarded as too low.

However, there are a number of exemptions from the hardcore main rule. Restricting the *licensor's* passive sales are not viewed as hardcore restraints, according to the Guidelines para. 99. The same is true for restrictions on active sales by the licensee, except in cases of selective distribution in art. 4 (2)(b)(vi), see 6.3.3. of this paper. As defined in the Guidelines to vertical restraints para. 50, active sales occur when a firm is "actively approaching individual customers inside another distributor's exclusive territory or exclusive customer group by for instance direct mail or visits".

Secondly, restrictions on the licensee's active or passive sales into the exclusive territory or customer group of the *licensor* is not on the hardcore list, cf. art. 4(2)(b)(i) and the Guidelines para. 100, as such restrictions are found to be pro-competitive.

Thirdly, a licensee will often have to make major investments when entering the market, and a major part of the investment is non-recoverable if he have to exit ("sunk" investments). To protect him in this critical phase, art. 4(2)(b)(ii) excepts restrictions on passive sales by other licensees into this licensee's exclusive territory or customer group for a period of two years from the hardcore list.

Further, art. 4(2)(b)(iii) block exempts agreements where the licensee can only use the licensed technology for captive use, i.e. for incorporation of the contract product into his own products, and not sell it to other competitors or producers. However, a ban on active or passive sales of spare parts to his own products is not exempted.

Art. 4(2)(b)(iv) concerns agreements where the licensee agrees to produce either only for one customer, or as an alternative source of supply. Such agreements are not hardcore, and when made between non-competitors, often not under art. 81(1) at all.

Likewise, when the licensee is a wholesaler, a contractual ban on him operating as a retailer and providing end-users with products, will often not be caught by art. 81(1), and is thus not part of the hardcore list, cf. art. 4(2)(b)(v) and para. 104 of the Guidelines.

6.3.3 Exceptions for selective distribution systems

The last exception from the hardcore list is found in art. 4(2)(b)(vi), and exempts agreements where the licensee is obliged to refuse sales to distributors who are unauthorised by the licensor. This way, the licensee becomes part of a selective distribution system. Such a system is allowed under EC competition law, since certain types of products cannot be sold anywhere, for a variety of reasons. In the landmark verdict of *Metro 1*[74], a retailer was denied to sell electronics from SABA in his self-service stores, which sparked off an art. 81-case. The ECJ clearly stated that selective distribution systems based on purely qualitative criteria are not caught by art. 81(1). Later dubbed 'the Metro-test', the product must be of a type that makes selective distribution necessary. In general terms, this includes product which are technically complicated, brand images and short-lived products as newspapers. Further, the qualitative criteria must be pure, and applied in a non-discriminatory way. Finally, any restrictions must not go further than necessary to obtain the aim of protecting the quality of the product.

However, in cases where no transfer of technology are involved, the TTBE cannot be applied, but the block exemption on vertical agreements. Even so, both the production level, the wholesale level and the retail level, or all three, can be affected by a licensing agreement, and thus be under the TTBE.[75]

7 Conclusion

As we have seen in this paper, the new TTBE have two overall aims. Firstly, it shall secure legal certainty for firms engaging in technology transfer in a new environment without any chance of getting an advance clearance. If the agreement falls under the safe harbour of the TTBE, neither the Commission nor national competition authorities will take action unless major changes are made to the agreement after implementation. By removing the old "grey" areas in the former block exemption, more

[74] Case 26/16 [1977] ECR 1875, [1978] 2 CMLR 44.

clarity has been sought while drafting the rules, at the same time as those falling outside the block exemption will still have a chance to assess their agreements based on art. 81 (3) EC.

Secondly, the new rules shall encourage licensing of IPRs by further broadening the scope of both the subject matter in a TT-agreement and the number of accepted agreement clauses which does not have as their object the distortion or of competition. By widespread licensing, competition both inter- and intra-brand, as well as inter- and intra-technology, will have a chance to grow, with lower prices for the consumers and a free movement of goods and services throughout the Community as a wanted result.

In order to reach these goals, the TTBE contains mainly two cumulative factors which have to be satisfied; a market share cap on the firms party to the agreement and banned hardcore restraints, concerning the very nature of the clauses inherit in the agreement. Also, the new Regulation distinguishes between agreements between competitors and non-competitors, as well as between reciprocal and non-reciprocal agreements, creating a more complex field of legislating, but at the same time creating a detailed map where it will be fairly easy to place an agreement.

We have seen that submissions made by companies and institutions on the proposed new rules have been taken into consideration by the Commission, and amended in several cases, especially is this true in terms of the new hardcore-list.

As for the criticism, some have argued that the new rules actually create less legal certainty for the companies. Especially "market leaders", who have no chance of getting below the market share thresholds in agreements with competing firms, have protested. Also, some have argued that the focus on market shares are anti-innovative, since the assessment process is "backward-looking"[76]; focusing on yesterday's market share rather than tomorrow's. This is particulary true in cases of completely new products and markets, the so-called innovation markets.

However, it seems to be the absence of hardcore restraints in technology transfer agreements that is the focal point of the Commission, stating several times both in the TTBE itself, its recitals and in the Guidelines that there is no presumption of illegality outside the market share thresholds. The new TTBE certainly benefits firms of slightly smaller sizes, allowing them to easily navigate themselves inside the safe harbour,

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[75] Cf. the Guidelines para. 39.

[76] See for instance World Competition Law and Economics Review, vol. 27, No.3 p 361.

without forcing them to wait for advance clearance as before. It can also be argued that firms of scale have the legal capability and economic stamina to examine their agreements more closely under art. 81(3).

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